

Restaurants Must Pass on Service Charge to Staff, or Pay Tax

CBDT asks field officials to examine balance sheet in cases of under-reporting or non-reporting of additional income collected in the name of tips

Our Bureau

New Delhi: Restaurants and hotels imposing service charge on customers in the name of tips but not passing them full to their employees could court trouble from taxmen. Central Board of Direct Taxes, the apex direct taxes body, has directed its field officials to examine balance sheet and expenditure statement of restaurants and hotels in cases where there is any under-reporting or non-reporting of additional income collected in the name of service charge.

The CBDT has said wherever it is found that the service charge rece-

pts have not been passed on to the staff or there is some under-reporting or non-reporting of receipts, it should be duly brought to tax.

"While framing assessments or carrying out verification under provisions of the Income Tax Act, 1961, in case of hotels and restaurants it is necessary to examine whether there is any under-reporting or non-reporting of additional income collected in the name of service charge," it said in a circular.

Service charge is supposed to be in the nature of 'tips' for hotel or restaurant staff and is sought to be collected on their behalf. But there have been reports of some restaurants and hotels not passing it to

Tip Of the Service

- » Taxmen looking to see if tips collected passed on to employees
- » Hotels and restaurants at times levy service charge
- » This is usually at 10% & mentioned on the menu



» **TAX OFFICIALS** to see balance sheets to check how these are being accounted

» **IF NOT PASSED** on, these should be treated as revenue and taxed

their staff. Service charge is not taxable and the amount of service charge levied is entirely at the discretion of restaurants and hotels. Usually, the rate is 10% and it is mentioned on the menu.

This follows a clarification by the

department of consumer affairs in April 2017 that service charge levied by restaurants and hotels is 'voluntary' and customers can refuse or pay according to their wish.

Subsequently, minister of consumer affairs, food and public distri-

bution Ram Vilas Paswan had tweeted on September 12, 2017: "In view of the seriousness of issue, department of consumer affairs has written to CBDT to consider inclusion of service charge while assessing tax".

Tax experts say industry will have to be prudent now in their treatment of the levy. "Such taxpayers would now have to act prudently by either eliminating such levy on the total bill or passing on its effect to the hotel/restaurant's workers," said Suraj Nangia, partner at Nangia Advisors LLP.

Vikas Vaidya, national leader tax at Grant Thornton India LLP, said from a commercial perspective, as this is not a government

mandated levy, consumers should have an option to pay the same depending upon their overall experience and the services received. "From a tax perspective, it may be prudent for the government to clarify its position for the employer and the employee, as well as under GST to avoid unnecessary dispute and litigation."

Amit Maheshwari, partner at Ashok Maheshwari & Associates LLP, said, "One has to see if this would result in higher tax revenues, since even currently non-payment of tips to staff in spite of collecting them increases profit and consequently the taxes. We expect a tighter tax scrutiny of the industry."

Service charge not distributed to workers by restaurants liable to income tax

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SERVICE CHARGE COLLECTED by hotels and restaurants but not passed on to staff and workers will be liable to income tax in the hands of such entities, the tax department has said.

The department has asked field offices to examine books of hotels and restaurants to see if there is any 'under reporting' or 'non-reporting' of service charge collected by them.

The missive from the Central Board of Direct Taxes (CBDT) came after the Ministry of Consumer Affairs flagged that some hotels and restaurants are collecting service charge from customers in a compulsory manner, which is in contravention with the guidelines issued by the ministry.



The ministry also said there is "every likelihood" that the service charge amount collected is not even distributed among staff and workers.

The CBDT asked field offices to examine whether there is any under-reporting or non-reporting of additional income collected in the name of service charge.

"The disclosure and disbursement details of service

charge transactions as contained in P&L (Profit & Loss) A/c, I/E (Income/Expenditure) statement and balance sheet should be critically examined to ascertain whether receipts from service charges are fully disclosed as part of the turnover of the hotel/restaurant or not," the CBDT said.

It said that in situations where it is found that receipts have not been passed on to

staff or workers by the hotel/restaurant or there is some under reporting or non-reporting, receipts should be duly brought to tax in the hands of concerned hotel/restaurant.

The guidelines said that the bill presented to the customer may clearly display that service charge is voluntary and the service charge column of the bill may be left blank for customers to fill up before making payment.

Nangia Advisors partner Suraj Nangia said: "These guidelines are going to increase the strain of the mischievous hotels/restaurant owners as it points out their misdeeds. Such taxpayers would now have to act prudently by either eliminating such levy on the total bill a amount or passing on its effect to the hotel/restaurant's workers."

